

This record is a partial extract of the original cable. The full text of the original cable is not available.

C O N F I D E N T I A L SECTION 01 OF 02 RANGOON 000079

SIPDIS

STATE FOR EAP/BCLTV, EB
COMMERCE FOR ITA JEAN KELLY
TREASURY FOR OASIA JEFF NEIL
CINCPAC FOR FPA

E.O. 12958: DECL: 01/10/2012

TAGS: [ECON](#) [EFIN](#) [BM](#)

SUBJECT: BURMA: THE ILLUSION OF ECONOMIC STABILITY

REF: A. RANGOON 30

[1](#)B. 02 RANGOON 1468

Classified By: CDA a.i., Ron McMullen for Reasons 1.5 (B,D)

[1](#)1. (C) Summary: Since last Fall, Burma has seen the formation of new government economic advisory committees, a relatively stable kyat, and slowing consumer price inflation. Could this mean the regime is finally taking real steps to improve the economic situation? Unfortunately not. The exchange rate stability is illusory, the slowing consumer price rises mask a still rampant inflation rate. As for the committees, nothing good can come of them. End summary.

Government Committees: Training Grounds for Corruption

[1](#)2. (C) As a sign of its earnest efforts to remedy the nation's economic woes, the regime established in September several committees to monitor and advise on the nation's economic crises. These green ribbon committees, all chaired by top SPDC members and military trustees, are ostensibly looking at issues ranging from fuel conservation to commodity price control. While this seems encouraging, local economists say that such a move is commonplace and rarely turns into legitimate reform. More likely, some opined, these committees end up as training grounds for young officers on how to take advantage of the country's economic distortions for their own benefit.

Exchange Rates: Pressure is Building

[1](#)3. (SBU) Nonetheless, statistics collected by the Embassy show a relatively stable dollar/kyat market exchange rate over the past two months. The kyat raced from 900 in August to 1310 kyat/dollar in mid-September before plateauing at about 1000 kyat/dollar from October through the end of 2002. This value of the kyat is still lower than it was at the beginning of 2002 (720 kyat/dollar), and is still 167 times below the official rate (6 kyat/dollar). However, it is significant that such stability could come, and endure, without any evident economic reforms or positive changes in the business climate.

[1](#)4. (SBU) As we reported in Ref B, this curious period of stability is largely due to the government's decision to remove a major distorting factor from the foreign exchange market. The military-directed Myanmar Economic Holdings, Ltd. (MEHL), not required like other importers to cover their import expenses with export revenues, had been a major consumer of black market dollars to fund its exclusive right to import diesel fuel and palm oil for cooking. These import privileges, unfortunately bred significant corruption and higher prices. Thus, the regime, in cooperation with MEHL's new leadership, decided in late 2002 to crack down on MEHL and re-assign the right to import diesel and cooking oil to state-controlled entities. This decision in a stroke reduced significantly the demand for "uncovered" dollars on the open market. The government also periodically fine tunes the exchange rate through "administrative measures" (e.g., arresting large money changers).

[1](#)5. (SBU) The government's increasing miserliness on the granting of import licenses also helps to explain the stability of the kyat. Over the past several months, importers have complained about regular GOB refusal of license requests or extremely slow approval. Also, they say, even approved licenses are regularly for 50 percent less than the amount requested. Reflecting this, the recorded value of imports fell throughout 2002 by about 35 percent, according to official statistics.

Prices: Consumer Goods Steady, but Inflation Roars

[1](#)6. (SBU) Despite a drop in the official value of imports, there has been no sharp rise in the cost of imported consumer goods in Rangoon. From October through December, the price changes of our basket of imported consumer items have been about the same, or in one case lower, than the overall monthly CPI increase, which itself has slowed over the past three months. The only significant increase in price in

December's basket came from cooking oil -- perhaps a reaction to the new government-controlled importing and distribution arrangement.

17. (C) A number of factors appear to explain this. First, importers tell us that they have kept their volume steady, despite tighter import controls, by shifting their purchases from better quality, more expensive Thai, Japanese, Korean, and western products to cheaper Chinese goods. Second, for consumer goods a virile black market here has kept the supply relatively steady, combined with some import substitution (particularly in snack foods and dry noodles) and some dip in demand commensurate with decreasing standards of living. Finally, the import statistics may be somewhat misleading as many importers underinvoice to bring in more product for their dollar's worth of export revenue, covering themselves by converting kyat earnings at the curbside market and moving it offshore through the black market exchange system (hon ti). However, importers tell us that Customs has been cracking down on this practice lately, unilaterally marking up the invoice or requiring proof in the form of export records from the country of origin.

18. (C) Furthermore, broader inflation remains a serious problem countrywide, especially when combined with stagnant wages and the eroding value of the kyat. We estimate the rate for Rangoon in 2002 at about 60 percent. One of the most serious causes is excess money supply due to the Central Bank's monetizing of chronic GOB budget deficits. This, combined with a weak banking sector and the depreciation of the kyat, has led business people to unload kyat and snatch up legal assets (especially real estate, cars, gold, and gems) as fast as they can. The resulting asset bubbles have been exacerbated by the boom in informal financial institutions that are investing in these same assets their surprisingly large deposits (see Ref A). The high cost of transportation and imported fertilizer and tractors, combined with supply and distribution problems have also kept rice prices at historic high levels. Likewise, the dysfunctional distribution system for fuel has led to steep price hikes for black market diesel and gasoline.

Comment

19. (C) In short, there is little evidence that the recently stabilized exchange rate has anything to do with any new stability in the economy. While regime policies imposing tighter import controls and reining in the greedy MEHL have helped economize on foreign exchange and have helped squeeze out some corruption from the trading system, there has been no real effort to deal with the excess liquidity generated by the central government's budget deficit and the still expanding operations of the unofficial financial institutions. Absent moves in these areas to deal with the rapidly expanding money supply, there is little that tighter enforcement of the GOB's current rules can do. As a consequence, most people are still looking to a sharp increase in the exchange rate this spring. Eighteen months ago, we forecast an exchange rate of 1800-2000 kyat/dollar by the end of Burmese FY 2002-03 (March 31). Now it appears that the exchange rate may come in at the low end of that range, but even that will represent a near doubling of the exchange rate against the dollar in one year -- not in any sense a sign of a stabilizing economy. End comment.

McMullen